No. 6835

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IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

JOHN FREULER, Administrator of the Estate of Louise P. V. Whitcomb, Deceased,
Respondent.

REPLY BRIEF FOR RESPONDENT.

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I. PRELIMINARY STATEMENT.

The court asked that the reply brief be confined to the two questions of law presented by the case. We, therefore, summarize those issues first in this reply (*infra*, pp. 2-49). Petitioner has frankly exceeded the leave given by the court regarding reply briefs (Pet. Rep. p. 1), and has discussed various matters outside of these two questions of law. We assume that the court will wish us to note them briefly as we have done below (*infra*, pp. 50-58).

II. ARGUMENT.

1. WHEN A TRUSTEE, ACTING UNDER A RESIDUARY DEVISE OR BEQUEST WHICH CONTAINS NO SPECIFIC DIRECTIONS ON THE SUBJECT, PURCHASES WASTING SECURITIES THE LAW IMPLIES AN OBLIGATION TO PROVIDE PROPER AMORTIZATION (Res. Br. pp. 6-25).

Primarily the question whether or not a depreciation reserve must be maintained by a trustee is one to be settled by the creator of the trust. In numerous cases, however, as in the case at bar, trusts have been created by wills with no specific directions on the subject. Like other questions of construction, the courts on this question have established certain principles.

Special cases as of the specific devise of wasting assets,

Perry on Trusts and Trustees, 7th Ed., Vol. II, par. 548 (Res. Br. p. 15);

In re Chapman, 66 N. Y. S. 235, 238 (Res. Br. p. 17);

Reed v. Longstreet, 71 N. J. Eq. 37, 63 Atl. 500 (Res. Br. pp. 20-21);

Gay v. Focke, 291 Fed. 721 (Res. Br. p. 21),

must be set aside as involving evidence or supposed evidence of a testamentary intent opposed to the general rule. The authorities have discussed three types of wasting assets:

1. Tangible depreciable property

Matter of Houseman, 4 Dem. 404 (Res. Br. pp. 7-8);

Hill on Trustees (Am. Ed.) 592-593 (Res. Br. p. 16);

Newbury v. Commissioner, 26 B. T. A. 101, 106-107 (Res. Br. pp. 23-24).

2. Bonds purchased at a premium

In re Gartenlaub, 185 Cal. 648, 652 (Res. Br. p. 9);

In re Stevens, 187 N. Y. 471; 80 N. E. 358, 359-360 (Res. Br. pp. 9-10);

New England Trust Company v. Eaton, 140 Mass. 532; 4 N. E. 69, 71-72, 74, 77 (Res. Br. pp. 10-12);

In re Allis' Estate, 123 Wis. 223, 101 N. W. 365, 368 (Res. Br. pp. 12-13);

Furniss v. Cruikshank, 230 N. Y. 495, 130 N. E. 625 (Res. Br. p. 13);

New York Life Insurance & Trust Co. v. Baker, 165 N. Y. 484, 59 N. E. 257 (Res. Br. p. 13);

Gould v. Gould, 213 N. Y. S. 286 (Res. Br. p. 13);

Kemp v. Macready, 150 N. Y. S. 618 (Res. Br. pp. 13, 18-19);

Dexter v. Watson, 106 N. Y. S. 80 (Res. Br. p. 13);

Curtis v. Osborn, 79 Conn. 555, 65 Atl. 968 (Res. Br. p. 13);

Ballantine v. Young, 74 N. J. Eq. 572, 70 Atl. 668 (Res. Br. p. 13);

In re Wells' Estate, 156 Wis. 294, 144 N. W. 174 (Res. Br. p. 13);

Perry on Trusts and Trustees, 7th Ed., Vol. II, par. 548a (Res. Br. p. 16);

Simon v. Commissioner, 10 B. T. A. 1186, 1188 (Res. Br. p. 25).

3. Valuable leaseholds

Healey v. Toppan, 45 N. H. 243, 266-267 (Res. Br. p. 13);

In re Hall's Estate, 224 N. Y. S. 376, 381 (Res. Br. pp. 13-14);

In re Murphy's Estate, 246 N. Y. S. 714 (Res. Br. p. 14);

In re Golding's Estate, 216 N. Y. S. 593 (Res. Br. p. 14);

Perry on Trusts and Trustees, 7th Ed., Vol. II, par. 548 (Res. Br. p. 15);

Hill on Trustees (Am. Ed.), 592-593 (Res. Br. pp. 15-16);

Gay v. Focke, 291 Fed. 721 (Res. Br. pp. 21-23).

In any such case the trustee makes the investment, purchases the wasting asset, for exactly the same reason that any other person makes an investment in such an asset. In every investment the investor has in mind two things, the ultimate return of his principal and meantime the receipt of an income. Where the investment is a wasting asset the investor requires that the periodical return from the investment be greater than in other cases; the investor must not only receive a periodic return commensurate with that which he would receive in other investments, but also an additional amount to refund some part of the principal invested. Precisely these considerations must be regarded by a trustee when he makes an investment of this kind. When the trustee has two sets of beneficiaries, life tenants entitled to the income during the term of the trust and remaindermen entitled to the principal on the termination of the trust, equity is done between the two classes of beneficiaries by giving to the life tenants the portion of the gross income received periodically which represents the true earning on the investment, and by retaining for the benefit of the remaindermen the portion of this gross income which represents a return of capital. With this fund the trustee sets up a depreciation or amortization reserve. The principal of this fund, of course, he may again invest and the life tenants are entitled to the earnings. The problem is the same whether the wasting investment be tangible property or intangible, like bonds selling above par and a leasehold worth more than the periodic rental.

Petitioner tries to distinguish between these different kinds of wasting investments (Pet. Rep. pp. 2-3). The effort is to place on one hand the cases of bonds purchased at a premium and on the other hand all other purchases of wasting assets. No such distinction is made by the authorities. As we have seen, all recognize that the same legal and economic problem is involved in each class of cases. Seeking to support his argument that bonds, the second class of wasting assets, should be treated differently from the first and the third classes (*supra,* pp. 2-4), tangible properties and valuable leases, petitioner says:

> "When bonds are purchased at a premium there is an immediate loss—a conversion of money into the promise of repayment of a lesser amount" (Pet. Rep. p. 3).

This is by no means true. No investor would make such a purchase, would face such an immediate loss. If the bond is ultimately paid no loss is involved, simply the capital has been returned partly in installments and the rest in the repayment of the par value. Apart from market fluctuations, the bond is worth no less the day or the instant after its purchase than it was before. Normally the purchaser could sell the bond immediately at the same price which he paid for it. Sometimes he is so fortunate as to be able to sell it at a greater price. Contrast this with an everyday transaction, the purchase of a notoriously wasting tangible asset. A new automobile is purchased from the agent. As soon as the buyer drives it out of the agency there is, in fact, a definite loss—in resale value, in insurable value. This is simply because a brand new car is worth more than a "used car." More or less the same is true in the case of the purchase of any tangible depreciable property. Undoubtedly the furniture installed in the Whitcomb Hotel was worth less the day after it was installed than it was the day before on the floor of the merchant's shop. If there were any distinction of the kind suggested by petitioner, every consideration is in favor of the loss being more immediate on the purchase of a depreciable tangible asset than it is on the purchase of a bond.

Pressing this same argument about depreciation of wasting assets, other than bonds, petitioner says:

> "Practically it may never be realized as a loss in any given case" (Pet. Rep. p. 3).

It is, of course, conceivable that market fluctuations might be such that tangible depreciable properties, an old hotel building, second hand hotel furniture, might at some time be saleable for more than their original purchase price. That, however, is a false quantity. The same argument was made, indeed, about bonds themselves.

> "This loss of the remainder-man may, however, be reduced if the life estate falls in before the bonds

mature, and while they are still quoted at a large premium."

In re Hoyt, 160 N. Y. 607, 55 N. E. 282, 285 (Res-Br. pp. 17-19).

There is simply nothing in the distinction suggested by petitioner between the various classes of wasting assets.

We agree with petitioner's statement regarding depreciation that:

> "Whether it shall be borne by life tenant or remainderman is primarily a question of the construction of the instrument creating the trust" (Pet. Rep. p. 3).

We submit, however, that in construing the instrument the court acts in accordance with settled principles. Petitioner concedes that:

> "it is quite clear that in California and probably a majority of the states the trustee purchasing bonds at a premium is obliged to reserve from income a sum sufficient to amortize the premiums paid so that the capital is kept intact. This seems to be the rule announced by the Supreme Court of California in *Estate of Gartenlaub,* 185 Cal. 648, 198 Pac. 299, and it is also the rule adopted by the Supreme Court of the United States in *New York Life Insurance Co. v. Edwards,* 271 U. S. 109" (Pet. Rep. p. 2).

Surely petitioner does not mean by this to state a rule of law peculiar to the purchase of bonds at a premium which would override testamentary intent as ascertained by the contruction of the will. All that this statement can be is petitioner's acknowledgment of a well recognized rule of construction which is just as applicable to the purchase of other kinds of wasting assets as it is to the purchase of bonds.

Petitioner cites this court's decision in *Gay v. Focke,* 291 Fed. 721 (Res. Br. pp. 21-23), as showing a disposition to apply to other kinds of wasting assets, specifically to a lease, some rule of construction different from that applied in the case of bonds. Obviously petitioner cites the case now without having given consideration to our discussion of the case (Res. Br. pp. 21-23). As there shown, the decision of this court in the *Gay* case applied to the Hawaiian leases the precise principles applied by other courts in regard to the amortization of other wasting assets. One lease had been bequeathed specifically. According to *Perry's* remark (Res. Br. p. 15) and the *Chapman* case (Res. Br. pp. 16-17) the life tenants would be entitled to the full income without any deduction for amortization (*supra,* p. 2). That is precisely what this court held regarding that lease. In the *Gay* case, however, there was also another lease which passed under a residuary bequest. The Hawaiian court held that that lease was subject to amortization in accordance with the general principles applied in the case of bonds and other wasting assets. The question was not raised on appeal. The cases which this court cited, however, in discussing the computation of this amortization, showed that it did not regard the decision of the Hawaiian court on this point as incorrect.

Passing to the construction of the Whitcomb will, petitioner says:

> "Certainly there is nothing in the will to indicate"

the testator's desire

> "that the corpus should be unimpaired" (Pet. Rep. p. 3).

We submit that there are two specific features of the will which indicate the desire to maintain the corpus. The first is the language in which the testator disposes of the income, to which he applies the term "interest" (R. 35). The second is the language with which he disposes of the remainder "of the *whole* three-thirds parts" (R. 35). General principles of construction, as we have said, do not require in a case of this kind affirmative evidence of the desire of the testator that those general principles be applied in the construction of the will. Nevertheless, short of express direction that a depreciation reserve be maintained, it is hard to conceive of any language which a testator might have used which could be more apt to require the application of these general principles of construction.

Most of the remainder of the matter under this first point in petitioner's reply brief seems pertinent in no way to the discussion of the general question of law, which was one of the two to which the court directed that our reply briefs be devoted.

Ainsa v. Mercantile Trust Co., 174 Cal. 504, 163 Pac. 898 (Pet. Rep. p. 3) is not a testamentary trust, involves no question of the rights of life tenants and remaindermen and has nothing to do with any question of depreciation or other treatment of wasting assets. Petitioner cites it as holding that the terms of the trust instrument govern the duties of the trustee. Such a decision can be of no assistance here where the question is one of construction of a will in which there is no specific direction as to the trustee's duties in connection with this particular problem.

Bryson v. Bryson, 62 Cal. App. 170, 175, 216 Pac. 391 (Pet. Rep. pp. 3-4) likewise involves no testamentary trust, no question of the rights of life tenants and remaindermen, no question of depreciation or other treatment of wasting assets. It states, indeed, that the trustee is bound by the provisions of the trust instrument, but it is of no assistance in our problem—the proper construction of the trust.

Petitioner cites Section 101 of the Probate Code (Pet. Rep. p. 4) to the effect that the will must be construed according to the testator's intent. Of course this does not mean that the courts are to make use of no established principles of construction in ascertaining the testator's intent. For if it did, all of the succeeding portions of the Probate Code, Sections 102-126, would be unnecessary. Petitioner misunderstands Section 163 of the Probate Code which he says

> "subordinates the provisions *of the code itself* to the testator's express intention" (Pet. Rep. p. 4).

The section reads:

> "The provisions *of this chapter* are in all cases to be controlled by a testator's express intention."

The chapter is chapter 8 of division 1. None of its provisions are in any way involved in the case at bar. Section 163, therefore, has no bearing whatever.

Departing still further from the specific question of law upon which the court asked the assistance of briefs, petitioner cites *In re Leupp,* 108 N. J. Eq. 49, 153 Atl. 842 (Pet. Rep. p. 4), in support of an alleged estoppel of the beneficiaries to question certain acts of the trustee in the knowledge of which they had accepted distributions of income for sixteen years. It is certainly late for petitioner to inject such a question into the case. The question was not raised before the board, is not presented by any of the assignments of error (Res. Br. pp. 56-59), nor by the corresponding "specification of errors" which petitioner inserted in his brief by amendment (Pet. Br. p. 11). A glance at the record, however, shows that there could be no such estoppel in the case at bar. Instead of receiving the income with knowledge of the trustee's acts as the beneficiaries did in the *Leupp* case, it appears that the objecting beneficiaries here, Napoleon Charles Louis Lepic and Charlotte de Rochechouart (R. 38), never have had a right to receive any of the income and never have received any of the income (R. 36-37). The fact that they were minors during most of this period does not appear directly from the record. It does appear, however, that their mother was born December 4, 1882 (R. 35). The eldest of them, therefore, may well have been born about 1903. That both of them were minors during the year 1921 and thereafter is a reasonable inference from the record. That neither of them at any time had any knowledge of the trustee's accounting methods is a matter on which the record is absolutely silent. As to the other remaindermen, Lydia L. Whitcomb and Louise A. F. E. Whitcomb, neither of them received any income prior to 1914. Their minority is an admitted fact in the case (Consolidated, Amended and Supplemental Petition, par.

1 (a) and 1 (b), R. 13; Answer, R. 29). Certainly there could be no question of estoppel on the part of the remaindermen in the case at bar.

Equally disconnected from the question of law as to which the court directed the briefs is petitioner's statement that

> "The orders of the probate court * * * do not in themselves stamp the distributions as unlawful" (Pet. Rep. pp. 4-5).

The order sustained objections to the account because no reserve or other provision for depreciation had been made (R. 39). It adjudged that specific amounts were proper amounts for depreciation during each of the years covered by the account (R. 39-40). It absolved the trustee from personal liability (R. 40-41). It ordered the recipients to repay the excessive amounts (R. 41). It required the maintenance of a depreciation reserve in the future (R. 41). We fail to see how a court could have been more plain in its expression of its intent to

> "stamp the distributions as unlawful" (Pet. Rep. p. 5).

All that petitioner can mean by this paragraph is that the court erred in absolving the trustee from personal liability. Assuming that error existed this, as the board said "is a matter between them and the trustee and the other parties interested in the trust" (R. 48). It certainly has nothing to do with the question of general law thoroughly briefed by us (Res. Br. pp. 6-25) but ignored in petitioner's brief (Res. Br. p. 25) to which the court ordered that these briefs be directed.

Still pursuing, not the question of law, but questions of fact regarding the administration of this particular trust, petitioner quotes our remark that

> "there was no depreciation question prior to 1913" (Res. Br. p. 29)

and retorts

> "Obviously depreciation was not created by the Sixteenth Amendment" (Pet. Rep. p. 6).

If the innuendo is intended that our concern about depreciation only exists in order to escape income tax, we must insist that the passage quoted by petitioner from our brief be read in connection with the earlier passage to which it referred.

> "For twenty-seven years from the time of A. C. Whitcomb's death in 1889 until 1906, when the fire resulted in a change in the investment policy of the trustee, no material part of the corpus of the trust estate was depreciable or a wasting asset of any other kind. The question of depreciation, therefore, did not arise. From 1906 until 1913 the trustee was engaged in various stages of the construction of the Whitcomb Hotel. Any attempt to base an argument, therefore, upon anything done by the parties to this trust in the treatment of depreciation prior to 1913 must fail. There was not and could not have been any question of depreciation before 1913" (Res. Br. p. 28).

All argument about the matter of depreciation prior to 1913 is beside the point. There is no finding by the Board of Tax Appeals (R. 36) that any depreciation existed prior to 1921, the year involved in this case. The only intimation that there was prior depreciation is the finding of the probate court, which shows that there was depreciation in the years from 1913 on (R. 40). Nowhere is there anything in the record showing that there was depreciation prior to 1913.

This court having ordered briefs on questions of law alone, we had hoped that further discussion of mere assertions of fact would be avoided. Yet we find under the discussion of this first law point a repetition of the attack on the decree of the probate court here (Pet. Br. pp. 2, 11, 15, 16, 21, 22, 32; Res. Br. pp. 28-29). The charge now is that the "decree of the probate court was for all practical purposes a consent decree" (Pet. Rep. p. 6). Again petitioner disclaims any charge of collusion (Pet. Br. p. 6, note 3). To us the charge and the disclaimer seem inconsistent. It is idle, however, to attempt an analysis. The fact is that the record contains no finding whatever tending in any way to impeach the order of the probate court. At the argument petitioner went outside of the record to urge this charge. At that time we offered to go outside the record and to state the facts obviously unknown to petitioner's counsel regarding the probate court procedure. This court properly declined to hear any such discussion. We assume that it will, therefore, disregard the baseless charge now made by petitioner.

Again without any bearing upon the general question of law on which the court asked assistance, petitioner goes outside of the record to discuss the proceedings pending regarding income taxes for the earlier years (Pet. Rep. pp. 6-7). He intimates the possibility that

> "*Whitcomb v. Blair* and the associated Board decisions" (Pet. Rep. p. 7)
>
> "established the law of the case" (Pet. Rep. p. 7)

and of

> "relying on the doctrine of *res judicata*" (Pet. Rep. p. 7).

Neither respondent nor his decedent was a party to *Whitcomb v. Blair*. They are not concerned with that case. Certainly it cannot be *res judicata* against respondent in any sense. So far as respondent is concerned it could not establish the law. Respondent obviously was entitled to his day in court.

Still staying outside the record, petitioner remarks:

> "it is peculiar that no effort was made to have *Whitcomb v. Blair and the associated Board decisions* reviewed by higher authority" (Pet. Rep. p. 7).

The court, we trust, will pardon our diversion from the record so far as to permit us to advise the court of something apparently unknown to petitioner, that is, that appropriate proceedings are pending in the district court against the Collector of Internal Revenue by respondent to review "the associated Board decisions" so far as respondent and his decedent are concerned in them. These proceedings have been deferred at the request of the United States attorney until the decision of this court upon this present appeal. So far, therefore, from "the associated Board decisions" being either *res judicata* or establishing the law of this case, the fact is that the ultimate decision of those cases depends largely upon the action of this court here.

Petitioner closes his discussion of this first point of law with the assertion that

> "the respondent has pointed to no direct authority" (Pet. Rep. p. 7)

on this general point of law. We submit that the principle being the same in regard to all kinds of wasting assets, all of the authorities cited by us on the point (Res. Br. pp. 7-25) are direct authorities in favor of our contention that in the absence of specific directions in the will the requirement of a depreciation reserve will be implied. Of our authorities,

> *Matter of Housman,* 4 Dem. 404 (Res. Br. pp. 7-8);
>
> *Hill on Trustees* (Am. Ed.), 592-593 (Resp. Br. p. 16); and
>
> *Newbury v. Commissioner,* 26 B. T. A. 101, 106-107 (Resp. Br. pp. 23-24),

specifically apply the general principle to the depreciation of furniture and improvements.

Petitioner says the question

> "arises under a Federal statute" (Pet. Rep. p. 7).

This is opposed to earlier language of the Commissioner.

> "The decisions of the local courts, however, as to the *distribution* of such items of income are important. They determine by whom the income should be accounted for. This makes it necessary that the *distributable* income be treated under class (4) and the capital gain or stock dividend under class (3) of section 219 (a)."
>
> O. 1013, 2 C. B. 181, 183-184.

The question, however, is not important since the federal law is settled in accordance with the state law, as to bonds on petitioner's own admission (Pet. Rep. p. 2), as to leases inferentially by the decision of this court (*Gay v. Focke,* 291 Fed. 721, *supra,* p. 8), and as to tangible property by the Board of Tax Appeals (*Newbury v. Commissioner,* 26 B. T. A. 101, 106-107, *supra,* p. 2). Petitioner repeats, however, his statements that the decisions cited in his earlier note (Petitioner's Br. pp. 20-21, note 2)

> "are believed to sustain beyond question the decision of the Court of Appeals in *Whitcomb v. Blair,* supra" (Pet. Rep. p. 7).

We agree that so far as *Whitcomb v. Blair* goes, it is in accord with the cases upon which petitioner relies (Pet. Br. pp. 20-21 note, Pet. Rep. p. 7), but as we have said (Res. Br. p. 34) the essence of *Whitcomb v. Blair* is that the court assumed without argument or discussion that, as a matter of fact, the depreciation was distributable. The construction of the will was not considered. It is on this matter of construction that this court has now asked the assistance of briefs. So far as those cases relate to the question of the maintenance of a reserve by the trustee, we can only repeat what we have already said that in those cases it was or was assumed to be the fact that the circumstances of the cases were not such as to require the application of the legal principles which are the subject of our present discussion (Res. Br. p. 34). Neither at the oral argument nor in his reply brief has the petitioner challenged this statement. At the oral argument, indeed, when the court asked the petitioner for his views on the general question of law as to the requirement of the maintenance of reserves by trustees, the petitioner replied that he had not completed his investigation of the authorities and knew of none on the point. If by his present statement (Pet. Rep. p. 7) with regard to the cases cited in the note in his earlier brief (Pet. Br. pp. 20-21, note 2) petitioner means to imply that those cases are in any way opposed to what we have said on that general question of law, it is obvious that such a claim is a mere afterthought. In any event these cases could not sustain any such claim. As petitioner discusses them in detail in the subsequent division of his brief, we have inserted our analysis of them under that head (*infra,* pp. 41-46). It shows definitely that they do not affect the general question of law as to the duty of trustees to maintain reserves.

We submit, therefore, that on the first question of law whether a depreciation reserve was required in the case at bar, the California law, the general law and the federal authorities are all in accord and all require such construction of the will.

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2. UNDER SECTION 219 OF THE REVENUE ACT OF 1921 THE MEASURE OF THE TAXABLE INCOME OF THE BENEFICIARY OF A TRUST IS THE AMOUNT OF INCOME DISTRIBUTABLE TO HIM PURSUANT TO THE INSTRUMENT OR ORDER GOVERNING THE DISTRIBUTION.

This section speaks of

> "income which is *to be distributed* to the beneficiaries periodically" (subdivision (a), paragraph 4).

In cases in which there is any income of the class described in paragraph 4 of subdivision (a) of this section, the fiduciary is required to include in the return

> "a statement of the income * * * which, pursuant to the instrument or order governing the distribution, is *distributable to each beneficiary, whether or not distributed* before the close of the taxable year for which the return is made" (subdivision (b)).
>
> "In cases under paragraph (4) of subdivision (a) * * * the tax shall not be paid by the fiduciary, but there shall be included in computing the net income of each beneficiary that part of the income * * * which, pursuant to the instrument or order governing the distribution, is *distributable* to such beneficiary, *whether distributed or not* * * * his *distributive share* of the income of the estate or trust" (subdivision (d)).
>
> "In the case of an estate or trust the income of which consists both of the income of the class described in paragraph (4) of subdivision (a) of this section and other income, the net income of the estate or trust shall be computed * * * except that there shall be allowed as an additional deduction in computing the net income of the estate or trust that part of its income of the class described in paragraph (4) of subdivision (a) which, pursuant to the instrument or order governing the distribution is *distributable* during its taxable year to the beneficiaries * * * there shall be included, as provided in subdivision (d) of this section, in computing the net income of each beneficiary, that part of the income * * * which, pursuant to the instrument or order governing the distribution is *distributable* during the taxable year to such beneficiary" (subdivision (e)).

In the above the phrases italicized are manifestly synonymous. They all refer to what ought to be done, rather than to what has been done. Other portions of the section also assist in the interpretation.

> "There shall * * * be allowed as a deduction * * * any part of the gross income which, *pursuant to the terms of the will or deed creating the trust,* is during the taxable year paid or permanently set aside for" certain charitable purposes (subdivision (b)).
>
> "In any other case * * * in determining the net income of the estate * * * there may be deducted the amount of any income *properly paid* or credited to any legatee, or heir, or other beneficiary" (subdivision (c)).

Under subdivision (b) the amount of the deduction is not the gross amount paid for the purposes named but the amount so paid "pursuant to the terms of the will or deed creating the trust." Again, under subdivision (c) the executor may take a deduction not for the amount of income actually paid to legatees, etc., but for "any income *properly* paid or credited to any legatee, heir, or other beneficiary." Subdivision (a) 4 is concerned not with the income distributed periodically but "which *is to be* distributed * * * periodically." Subdivisions (b), (d) and (e) deal not with what is distributed, but with what is *"distributable * * * whether or not distributed."* In principle the provisions concerning the income of trusts which is to be distributed to the beneficiaries periodically (subdivisions (a), (b), (d) and (e)) are based on the same policy as that of subdivision (b) regarding charities and subdivision (c) regarding decedents' estates. The underlying theory is that taxes are determined, not by the physical facts concerning the payment of the money, which might be affected by mistakes of the parties, either as to law or fact, or by the desire of the parties so to adjust these matters as to escape income tax, but by the legal rights and duties of the parties.

Our construction is in accord with the general policy of the income tax laws as shown by the various laws and the regulations under them.

The provisions of the Revenue Act of 1913 were very simple:

> "Guardians, trustees, executors, administrators, agents, receivers, conservators and all persons * * * acting in any fiduciary capacity, shall make and render a return of the net income of the person for whom they act, subject to this tax, coming into their custody or control and management, and be subject to all of the provisions of this section which apply to individuals" (section II, subdivision D).

"Trustees" are grouped here with "agents." The conception is that "they act" for the beneficiary. As soon as the trustee receives income which is distributable to any particular beneficiary the tax is imposed on the beneficiary just as if this receipt by the trustee were a constructive receipt by the beneficiary. On this theory, of course, it is immaterial when, if ever, the trustee actually passes the income over to the beneficiary. Neither overpayment by the trustee nor underpayment could have any effect upon tax liability. This theory was recognized by the Commissioner's rulings under the 1913 Act. Thus the Commissioner has said:

"Said fiduciary acts for and in behalf of the beneficiaries of said trust."

T. D. 1906.

See also:

T. D. 1911;

T. D. 1943.

"as each such fiduciary acts solely in behalf of the beneficiaries of the trust."

Regulations 33, art. 72, T. D. 1944.

See also:

T. D. 1961;

T. D. 1987;

T. D. 2090;

T. D. 2137;

T. D. 2231.

The Act of 1916

"Provided, that where the income is *to be distributed* annually or regularly between existing heirs or legatees, or beneficiaries the rate of tax and method of computing the same shall be based in each case upon the amount of the individual share *to be distributed*" (section 2, subdivision (b), paragraph 4).

The same provision is found in the Revenue Act of 1917, section 2, subdivision (b), paragraph 4.

Under these laws, the beneficiary was taxable, not with the amount *distributed* to him, but with the amount *to be distributed* to him. For the rest of the income the fiduciary paid the tax. The policy was established early that but one tax was to be collected on the net income of the estate where under the law the trustees had paid it.

T. D. 1906;

Regulations 33, article 75, T. D. 1944.

> "The income of the estate being thus freed of income tax liability may thereafter be dealt with without further regard to income tax requirements."

Regulations 33, article 29, revised January 2, 1918.

An important decision illustrating this principle is that embodied in the letter from the Acting Commissioner to the Corporation Trust Company, dated March 24, 1917 (Corporation Trust Company 1918 Service, pp. 366-367, 1919 Service pp. 141-142). There had been a devise in trust, the decedent dying in September, 1913. Until 1916, however, distribution was impracticable. At that time the shares of the net income during the earlier years 1913, 1914 and 1915 were ascertained. The fiduciaries were then directed to make fiduciary returns in 1916 for the earlier years, reciting the interests of the beneficiaries. The beneficiaries were directed to make amended returns for the earlier years where their income was such as to require returns. The fact that actually a large amount of income was distributed in 1916 did not justify the imposition of a higher tax in that year upon all of that income. The income was allocated to the years in which it was *distributable,* rather than the one year in which it was *distributed.*

The Act of 1918 was in this respect very similar to the Act of 1921 involved here. The pertinent provisions of subdivision (a) of Section 219 of the two acts are identical. There is a slight variation in subdivision (b), as shown by quotations in parallel columns from these two acts:

"Sec. 219. (b) The fiduciary shall be responsible for making the return of income for the estate or trust for which he acts. The net income of the estate or trust shall be computed in the same manner and on the same basis as provided in section 212, except that	"Sec. 219. (b) The fiduciary shall be responsible for making the return of income for the estate or trust for which he acts. The net income of the estate or trust shall be computed in the same manner and on the same basis as provided in section 212, except that
there shall also be allowed as a deduction (in lieu of the deduction authorized by paragraph (11) of subdivision (a) of section 214)	(in lieu of the deduction authorized by paragraph (11) of subdivision (a) of section 214) there shall also be allowed as a deduction, without limitation,
any part of the gross income which, pursuant to the terms of the will or deed creating the trust, is during the taxable year paid	any part of the gross income which, pursuant to the terms of the will or deed creating the trust, is during the taxable year paid
to	
or permanently set aside for the United States, any State, Territory, or any political subdivision thereof, or the District of Columbia, or any corporation organized and operated exclusively for religious, charitable, scientific, or educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private stockholder or individual; and	or permanently set aside for the purposes and in the manner specified in paragraph (11) of subdivision (a) of section 214.
in cases	In cases
under	in which there is any income of the class described in

paragraph (4) of subdivision (a) of this section the fiduciary shall include in the return a statement of	paragraph (4) of subdivision (a) of this section the fiduciary shall include in the return a statement of
each beneficiary's *distributive share* of such net income	the income of the estate or trust which, pursuant to the instrument or order governing the distribution, is *distributable* to each beneficiary,
whether or not distributed before the close of the taxable year for which the return is made" (Act of 1918).	*whether or not distributed* before the close of the taxable year for which the return is made" (Act of 1921).

The passages in subdivision (c) use identical language.

Subdivision (d) differs in the two acts by the same change of language which we have seen in subdivision (b). There is no subdivision (e) in the 1918 Act.

Interpreting these sections the regulations say:

> "Where the tax has been paid on the net income of an estate or trust by the fiduciary, such income is free from tax when distributed to the beneficiaries" (Regulations 45, article 344).

> "In the case of (a) a trust the income of which is *distributable* periodically * * * and (c) an estate of a decedent before final settlement as to any income property paid or credited as such to a beneficiary, the income is taxable directly to the beneficiary or beneficiaries. Each such beneficiary must include in his return his distributive share of the net income, even though not yet paid him" (article 345).

Note that in these regulations the language of paragraph 4 of subdivision (a) section 219, "income which is to be distributed," language which was identical in the 1916, 1917, 1918 and 1921 Acts is here paraphrased as "income * * * distributable periodically." Note also that in the act the phrase "income which is to be distributed" is used as synonymous with the "beneficiary's distributive share of such net income" and that in the regulations the phrase "income * * * distributable periodically" is used as synonymous with "his distributive share of the net income." In this regulation, therefore, we find the word "distributable" which was later taken into subdivisions (b), (d) and (e) of the 1921 Act.

Note also that the regulation uses the phrase "income properly paid or credited as such to a beneficiary" found in subdivision (c) of both the 1918 and 1921 Acts as synonymous with "his distributive share of the net income" and, therefore, with the word "distributable."

We find, therefore, that the word "distributable" in the 1921 Act was taken from the regulations under the 1918 Act, that as there used it is equivalent to the phrase "to be distributed" and also to the phrase "*properly* paid or credited." Under these circumstances the word was written into the Act of 1921. Congress will be taken to have used the word in the same sense in which it was used in the regulations.

Brewster v. Gage, 280 U. S. 327.

The 1918 Act, with this regulation made under it, therefore, furnishes the genesis of all the significant parts of the provision in the Act of 1921 we are considering. The provision is:

> "The income of the estate or trust which, *pursuant to the instrument or order governing the distribution,*[1] *is distributable*[2] to each beneficiary *whether or not distributed*[3]."

The source of each of these three expressions is as follows:

1. "Pursuant to the instrument or order governing distribution" is generally equivalent to "pursuant to the terms of the will or deed creating the trust" as found in the first portion of section 219 (b) of the 1918 Act.

2. "Distributable" is found in article 345 of Regulations 45 issued under the 1918 Act.

3. "Whether or not distributed" is found in the latter portion of section 219 (b) of the 1918 Act.

Regulations 62, issued under the 1921 Act, contain provisions in identical language with those we quoted from Regulations 45. There is also Article 347 which applies subdivision (e) of Section 219, the new subdivision in the Revenue Act of 1921.

The parallel between the first and the second portions of Section 219 (b) of the Revenue Acts of 1918 and 1921 is very close. We have seen the pertinent language in the second portion of the subdivision as it appears in the 1921 Act is taken from the earlier portion as it appears in both the acts. These provisions have been construed by the Board of Tax Appeals.

In *McClung v. Commissioner,* 13 B. T. A. 335, there was a will leaving the residue to the university. The heirs contested. The university arranged a compromise with the heirs under which the will was admitted to probate, and the university agreed that the heirs should receive one-half of the residue. The Board held that it made no difference that only half of the residue ultimately went to the university. Under the will it should all have gone to the university. The Board, therefore, allowed the deduction of the whole of the residue under the first portion of Section 219 (b). On the analogy of this decision a court, construing the second portion of Section 219 (b) of the 1921 Act, would say that although the amount was not actually *distributed,* nevertheless because it was *distributable* it was deductible by the trustee.

But the converse has also been held in regard to the deduction under the first portion of Section 219 (b).

In *Appeal of Estate of Tyler,* 9 B. T. A. 255, the executors had actually paid a certain portion of the income to the university. The Board held, however, that properly construed the will did not require this payment and, therefore, that it was not deductible. On the same analogy income *actually distributed* could not be deducted by the fiduciary if, as a matter of law, it was *not distributable.*

The same was held in *Heywood v. Commissioner,* 11 B. T. A. 29. The executor there made a payment to the Near East Relief, not because of any provision in the will, but because of a prior commitment of the testator. The Board held again that since the will did not direct the payment, the payment was not deductible.

These cases have been followed in construing Section 219 (c).

Sevier v. Commissioner, 14 B. T. A. 709, 717.

Petitioner repeats the suggestion he made at the oral argument that this section

> "which requires the inclusion in the income of the beneficiaries of such sums as are distributable

whether distributed or not only requires recourse to the term 'distributable' where the amounts are not actually distributed'' (Pet. Rep. p. 8).

This is directly opposed to the position taken in petitioner's opening brief, where one of his main points was:

> ''The distribution of the income to life beneficiaries, including respondent's decedent, was controlled in fact and in law by the terms of the deed of trust [1] executed in 1889'' (Pet. Br. p. 16).

At the argument petitioner said he knew of no case supporting this suggestion. He now concedes

> ''the absence of any case presenting quite the same fact situation'' (Pet. Rep. p. 8),

but expresses the belief that his construction

> ''finds considerable support in certain cases referred to in our principal brief and at oral argument'' (Pet. Rep. p. 8).

He does not say what the cases are which he believes support this view, nor does he point out wherein he thinks they support his view. He does not question the demonstration we made at the oral argument and now repeat that the construction suggested by petitioner then and now is directly contrary to the two decisions in one of the cases he himself cites.

> *Fidelity & Columbia Trust Co. v. Lucas,* 52 F. (2d) 298, 1932 C. C. H., Vol. III, par. 9167 (Pet. Br. pp. 32-35; Res. Br. pp. 41-43).

In that case the court held that under the will the income was not properly distributable. It, therefore, disregarded

1. Will.

what the trustee actually did and held under the second portion of Section 219 (b) that the tax had to be based upon what was *distributable.* We pointed this out at the oral argument. Petitioner does not attempt to meet what we said there (Pet. Rep. p. 15). This is the precise situation which exists in the case at bar. The only difference between the two cases in this regard is that in the case cited the disregarding of the actual distributions and the taxing of the whole income to the trustee resulted in a higher tax than would have been paid if the tax had been levied in accordance with the actual distributions which were divided among several beneficiaries. In our case, owing to the fact that the trustee has distributed all the net income of the trust and, in addition thereto, the depreciation and the capital losses (R. 129-131), the trustee had no net income in the reduction of which either the capital losses or the depreciation could have been applied. If the Commissioner can succeed in taxing the beneficiaries upon the total amount of distributions, including the depreciation, leaving the trustee with the bare right to apply depreciation and capital losses in reduction of a nonexistent capital net income, the result will be that the family interested in this trust will be taxed upon a greater sum than the total net income of the trust (Res. Br. p. 56, *infra,* p. 39). In such a situation it is to the advantage of the government to look at the amount actually distributed, rather than at the amount distributable. In the *Fidelity* case it was to the advantage of the government to look at the amount distributable rather than the amount distributed. The fact, however, that in one case it is to the advantage of the government to construe the statute one way and in another case another way does not mean that the courts will in every case disregard prior constructions and take the view most favorable to the United States. The language has a definite meaning and that meaning must be applied, whether it helps the tax gatherer or the taxpayer.

Petitioner departs from any question of construing this particular language and cites *Corliss v. Bowers,* 281 U. S. 376, 378, as supporting his statement

> "that what is subject to a man's unfettered command *is income to him*" (Pet. Rep. p. 8).

That is certainly not what Mr. Justice Holmes said in the case in question. What he said was:

> "The income that is subject to a man's unfettered command and that he is free to enjoy at his own option *may be taxed to him* as his income" (p. 378).

The statement was made in sustaining the constitutionality of subdivisions (g) and (h) of Section 219 of the Revenue Act of 1924 regarding income from revocable trusts. What the court held was that under the circumstances it was constitutional for Congress to impose this tax upon Corliss, even though the money was not actually his income. The court certainly did not say that the money was the income of Corliss. If the money actually had been the money of Corliss, of course Sections (g) and (h) of the Revenue Act of 1924 would have been unnecessary and the court would not have had to pass upon their constitutionality. In the *Corliss* case, while the money was not the taxpayer's income, nevertheless it was money to which he could legally obtain unquestioned title without any obligation to refund to anyone. That is, he could make it his income. In our case, whatever the decedent got through the overpayments, it was simply a mistake and she was lawfully obligated at all times to rectify it.

Still avoiding discussion of the specific question of construction on which the court asked briefs, petitioner cites *Cleveland Railway Company v. Commissioner,* 36 F. (2d) 347 (Pet. Rep. p. 8). That case is quite different. The essence of it is that the court held that the "interest fund" to which the excess income was devoted was in fact and in law the property of the taxpayer. It was, said the court,

> "a reserve fund created to effectuate the purposes of petitioner's franchise, one of which was to pay to the stockholders a fixed annual return on their investment."

There was no obligation in that case to return the money. There was no question there of money paid under mistake.

Another case entirely extraneous to the construction of Section 219 upon which the court asked briefs is the next one cited, *Ford v. Commissioner,* 51 F. (2d) 206 (Pet. Rep. p. 8; Pet. Br. pp. 35-37; Res. Br. pp. 43-46). The case is analyzed fully in our earlier brief and distinguished at length (Res. Br. p. 46). Petitioner does not undertake in his reply to answer what we said about it there. It certainly has no bearing on the question of construction and we shall not detain the court with it further.

Another case cited by petitioner which has no relation whatever to the question of construction is *Lucas v. American Code Company,* 280 U. S. 445. It deals with a matter of accrual and, therefore, can have no bearing upon the instant case which has to do with returns made on the cash basis. At any rate it cannot affect the construction of the express language of Section 219. It has nothing to do with any question of trusts. If it were applicable to the present situation and if the positive language of Section 219 were to be disregarded, then even if we could assume the actual amount distributed to the decedent in excess of the amount distributable to her in some way became income, nevertheless, immediately upon its receipt the obligation arose to refund it as money paid under mistake. The *American Code* case would have permitted respondent to deduct from the gross income the amount so refunded. This is within the express language of Mr. Justice Brandeis, who delivered the opinion of the court, saying:

> "Exception is made however, in the case of losses which are so reasonably certain in fact and ascertainable in amount as to justify their deduction" (p. 449).

He distinguishes carefully between such a case and the *American Code* case, which involved a mere unliquidated claim for breach of contract.

Petitioner refers to

> "the deduction of reserves to meet anticipated obligations" (Pet. Rep. p. 8),

instancing

> "bad debts" (note 5).

Of course, a bad debt is not an obligation of the creditor. The reserve which the creditor sets up is merely to take care of a loss which he feels may or may not occur in the future. The decedent in the instant case had no such problem. Being charged with knowledge of the law, she is deemed to have known that the depreciation distributed to her but not distributable was refundable. It was not a question of a possibility; it was a present actual obligation.

Petitioner speaks of this money erroneously distributed as

> "actual income" (Pet. Rep. p. 8).

It is clear that money received under such circumstances cannot properly be denominated "actual income." Petitioner assumes an obligation on the part of taxpayers

> "to report as income cash which he has in fact received and retained for his own purposes during the taxable year" (Pet. Rep. pp. 8-9).

"Cash which he has in fact received and retained for his own purposes during the taxable year" must include gifts and borrowed money. The very purpose of borrowing money from a bank is to get money which the borrower may receive and retain for his own purposes. It does not follow that either gifts or borrowed moneys are income or returnable as such. The very idea of income involves the idea of

> "gains, profits, and income * * * salaries, wages or compensation for personal service * * * interest, rent, dividends."
>
> Revenue Act of 1921, Section 213 (a).

See also

> Revenue Act of 1913, Section II, subsection B,

and corresponding sections of the other income tax acts. Borrowed money, money received under a mistake and which is to be returned, is certainly not income.

Petitioner seems to urge his construction of the statute because

> "a departure from this sound policy would pave the way for grave abuses" (Pet. Rep. p. 9).

It is clear that there can be no abuses so long as the taxability of the individuals concerned is not made to depend, upon actual distributions which may be affected by the whim of the parties, by their mistake, as here, or by a desire so to adjust their affairs as to get the lowest tax rate, as may have been the situation in the *Fidelity and Columbia Trust Company* case, *supra,* pp. 29-30. When the amount of tax has to be computed upon the amount distributable in accordance with the legal rights of the parties, no room is left for chicanery. On the other hand, if the amount deductible by the trustee and taxable in the hands of the beneficiary can be increased beyond the amount actually distributable, merely by the parties themselves arranging illegal distributions of income, the result will be that whenever the parties find themselves in this situation the government can be deprived of its revenue. The only construction of Section 219 which could open the way to abuses is the very construction which the government now urges here.

No more pertinent to the specific question of statutory interpretation, about which the court asked the assistance of briefs, is petitioner's discussion of what we said about the injustice of the petitioner's demand here (Res. Br. p. 56). Petitioner's statement that

> "all applicable statutes of limitation have long since run" (Pet. Rep. p. 9),

is, of course, without foundation in the record. Probably what petitioner means is somewhat as follows: It is conceivable that a trust might exist in which there was both income periodically distributable to the beneficiaries and income which the trustee was obligated to accumulate. This is the kind of case that Section 219 (e) was designed to cover. Under that statute the trustee deducts the distributable income from his return and the beneficiaries return distributable income; both the trustee and the beneficiaries pay taxes. In such a case, if at the outset the trustee overstated the distributable income, he would pay at the outset a lower tax than the correct amount. The beneficiaries, on the other hand, would be assessed with more than the correct amount. If the government were to allow the statute of limitations to run on any additional assessment against the trustee, and thereafter the beneficiaries were to raise the question of the correct amount of income distributable, it might be inequitable for the beneficiaries to get their excessive tax refunded so long as the trustee did not pay the additional tax admittedly due from him. This apparently is the kind of case which the petitioner has in mind. There is nothing whatever in the record to intimate that any such inequity could exist here. No such inequity was pleaded in the answer (R. 29-31). There is no assignment of error that raises the point in any way (Res. Br. pp. 56-59). The record, indeed, shows exactly the opposite. The trust was not of the character to which Section 219 (e) is applicable. The trustee's account shows that the entire net income was paid out to the various beneficiaries (R. 121, 122) during the year in question. There could never have been any income tax upon the trustee. The statute of limitations upon the trustee's income tax, therefore, is a matter absolutely immaterial. It could make no difference whether the record showed that the statute of limitations had run or not. However, in order to avoid any question that any inequity is sought in this case, we append a specific waiver by the trustee of the statute of limitations for the year here involved.

Petitioner says:

> "* * * the trustee was allowed precisely the amounts involved in this and associated cases as deductions in returning trust income" (Pet. Rep. p. 9).

If this means that these deductions were allowed in the return which the trustee made under the latter portion of Section 219 (b):

> "A statement of the income of the estate or trust which, pursuant to the instrument or order governing the distribution, is distributable to each beneficiary"

then the statement is correct. But petitioner apparently means that the deduction was made in computing

> "trust income upon which the trustee was taxable."

There is nothing in the record upon which any such statement could be based. The record shows clearly that the trustee had no undistributable income upon which he was taxable.

The effect of the decisions favorable to the United States, in *Roxburghe v. Burnet,* 58 F. (2d) 693 (Pet. Br.

p. 21, note; Pet. Rep. p. 12), is undoubtedly to work an injustice. If, in the *Roxburghe* case, the taxpayer had owned the buildings outright she would have been taxable only upon the total net income, that is, upon the net rents less the depreciation. The separation of legal and equitable interests due to the Roxburghe trust had the effect in that case of obligating the trustee to pay out all the rents to the taxpayer, without any deduction for depreciation. The essence of the Roxburghe decision is that the taxpayer, therefore, had to pay an income tax based upon the whole rents, without any deduction for the depreciation. The trustee, indeed, would have been permitted to deduct the depreciation from any undistributable income which the trustee had. The difficulty was, however, that in the *Roxburghe* case, as in the case at bar, all the net income was distributable and there was no net income to which the trustee could apply any depreciation deduction. This was an injustice. The injustice was apparent and was corrected by the Revenue Act of 1928 (Res. Br. pp. 32, 33). The injustice in the *Roxburghe* case which, as we say, was corrected by the Act of 1928, consisted in this, that the testator, thinking to protect and provide for his child by creating a trust, had really created a situation under which the income tax payable by the child was greater than if he had left her the property outright.

In our case, however, the injustice is even more apparent. The testator here was not guilty of the indiscretion of the testator in the *Roxburghe* case. His testamentary provisions were not such as to require the trustee to distribute the depreciation reserve in addition to the whole net income of the trust (*supra*, pp. 2-18). If the trustee had followed the testamentary directions and the legal implications from them, he would have distributed only the net income after deducting depreciation, and the beneficiaries would have been obligated only to pay a tax upon what they received. The trustee, however, was ill-advised. He distributed more than the amount distributable; he paid out the depreciation reserve. When the error was discovered, it was remedied. In the meantime, however, and because of the trustee's error, the beneficiaries are asked to pay this tax, greater than the aggregate amount that would have been paid if there had been no trust, greater than the amount which would have been paid if the terms of the will had been obeyed.

Petitioner says:

> "The 'rank injustice' which respondent fears is simply the payment of a tax when it is due" (Pet. Rep. p. 9.

That is certainly not our contention. We agree, however, with the Congress that passed the Revenue Act of 1928 that it is injustice that a trust created for the benefit of a widow and children should so operate as to increase their taxes over what they would have been if the property had been left to them outright, and we repeat that it is rank injustice to attempt to impose such a tax where the trust itself was not such as to involve the beneficiaries in this technical legal difficulty, but where the mistaken acts of the trustee, in perfect good faith, are being seized on by the taxing authorities to create an additional tax burden on the beneficiaries.

Petitioner adds:

> "that if the income in question is not taxed as the result of this and associated proceedings, it will pass, tax free, a *gift by the Federal Government to citizens of a sister republic*" (Res. Rep. p. 9).

One error is apparent in this statement. These particular excess payments of undistributable funds were not income, never have been income and are not income now. They were simply payments made by mistake out of the capital of the trust fund. In no event, however, can it be said that such funds are "a gift by the Federal Government." The maker of this gift was the testator, "Adolphus Carter Whitcomb, of the City and County of San Francisco, State of California, United States of America" (R. 75). He set apart the capital of this trust fund for the benefit of his widow and children. The trustee, in good faith, thought he was following the testator's directions in making these payments. This was a mistake. It operated to the detriment of the remaindermen; they objected, and the mistake has been rectified. In any event, however, there is here no "gift by the Federal Government."

Petitioner cites *United States v. Sullivan,* 274 U. S. 259, as refuting

> "Any suggestion that money illegally distributed is for that reason not subject to income taxation" (Pet. Rep. p. 9).

The *Sullivan* case merely held that a bootlegger had to pay income tax on his ill-gotten gains. A bootlegger's profits, of course, are income, entirely apart from the illegal nature of the consideration by which he earns them.

The whole intent of the transaction between him and his customers is that he shall keep his earnings. Essentially, they are earnings just as much as the emoluments of a lawful trader. In our case, however, there is no illegality in the transaction by which the improper distributions were made by the trustee to the beneficiaries. It was simply a mistake. The law requires that the money be returned in order to correct the mistake. It is not illegality in the sense of moral taint which requires the return of the money. It is simply the fact of payment under mistake.

Petitioner now claims (Pet. Rep. p. 9) that the group of decisions theretofore cited by him (Pet. Br. pp. 20, 21, note) sustain the construction of Section 219 which he suggested at the oral argument. The court will remember that when he suggested this construction, the court asked him whether he knew of any authority sustaining it, and he replied then in the negative. His present contention that the cases then in his brief sustained this construction is clearly an afterthought. His detailed analysis of the various cases (Pet. Rep. pp. 9-12) does not show that any one of them sustains the suggested construction. His statement at the oral argument that he knew of no authorities in support of that construction was correct. His present claim in regard to these authorities is incorrect.

Baltzell v. Mitchell, 3 F. (2d) 428 (Pet. Br. pp. 19-21, note; Pet. Rep. pp. 9, 10), and its companion case, *Baltzell v. Casey*, 1 F. (2d) 29 (Pet. Rep. pp. 9, 10), certainly are no authority for petitioner's suggested construction of Section 219 of the Revenue Act of 1921. The Revenue Act of 1921 was not involved. It is true that Section 219 of the Revenue Act of 1918 was applied. In this application, however, there was no suggestion that the beneficiary was taxable for anything more than the amount of income *distributable* to him in accordance with the terms of the trust. In that case the trustee had suffered certain capital losses by the sale of securities. These were similar to the losses which were the subject of the second portion of the remaindermen's objections to the trustee's account here (R. 131; Res. Br. pp. 29, 30). The decision of the Federal Court in the *Baltzell* case was the same as that of the State Court in this case, that is, that the income of the beneficiaries of the trust could not be decreased by reason of these capital losses, and, therefore, that they could not be deducted in ascertaining the amount *distributable.* The case has nothing to do with any question of depreciation or with petitioner's suggestion as to the construction of Section 219 of the Revenue Act of 1921. It has no bearing upon either of the points upon which this court asked the parties to file briefs.

Codman v. Miles, 28 F. (2d) 823 (Pet. Br. pp. 20, 21, note; Pet. Rep. p. 10), is also beside the point. That case involved no question of depreciation of the trust or even losses of the trustee. This appears from the passage which petitioner quotes:

> "There is no destruction or diminution by use of the property which furnishes the source of the income" (Pet. Rep. p. 10).

What the taxpayer was claiming was that as the end of her equitable life estate approached, the value of that estate diminished. She was seeking to deduct from her distributable income under the trust an allowance for depreciation of her equitable life estate. Very clearly, the case has no bearing upon either of the points on which the court has asked for briefs here. It has nothing to do with the question whether a trustee shall or shall not maintain a reserve to cover depreciation. It has nothing to do with the question whether under Section 219 of the Revenue Act of 1921, a beneficiary is to be taxed with income distributed to him in excess of the amount properly distributable.

Abell v. Tait, 30 F. (2d) 54 (Pet. Br. pp. 20, 21, note; Pet. Rep. pp. 10, 11), is also of no value here. It resembled *Baltzell v. Mitchell,* (*supra,* p. 41), in that it concerned the effect of capital losses on the part of the trustee. It reached the same result. It involved the Revenue Act of 1918 as distinguished from that of 1921. It has nothing to do with either of the questions on which this court has asked for briefs. It certainly does not pass in any way upon the question of maintenance by a trustee of a reserve for depreciation. Equally clearly, it does not pass upon petitioner's suggested construction of Section 219 of the Revenue Act of 1921.

Kaufmann v. Commissioner, 44 F. (2d) 144 (Pet. Br. pp. 20, 21, note; Pet. Rep. p. 11), is also foreign to the issues of this case and the two points upon which the court has asked for briefs. In that case the testator devised a legal life estate to his widow. There was no trust. The widow gave certain of the property to her sons. Much of the case is devoted to a discussion as to whether this gift was effectual. That discussion, of course, has nothing to do with the case at bar. Among the assets were four buildings; two stood in the name of taxpayer's sons, a third stood in the name of the executors, and the fourth was in the taxpayer's own name. The taxpayer claimed the right to deduct depreciation on all four of them. As to the first three, this claim was based in some way upon Section 219 (d) of the 1918 and 1921 Acts. The court did not sustain the claim, but held that as between life tenant and remaindermen, depreciation was the loss of the remaindermen. As to the fourth property, the court held the taxpayer was entitled to depreciation except for the fact that she failed in proof of value. There is nothing in the case relating to the duties of a trustee in regard to the maintenance of a depreciation reserve. There is nothing in the case supporting any such construction of Section 219 of the Revenue Act of 1921 as that for which petitioner now contends.

Hubbell v. Burnet, 46 F. (2d) 446 (Pet. Br. pp. 20, 21, note; Pet. Rep. p. 11), is also beside the point. A trust was created by deed. The trustee actually set up a depreciation reserve and withheld that amount from the beneficiaries. The court quoted Section 219 (d) of the Revenue Act of 1921, and held that the beneficiaries were taxable, not merely upon the amount *distributed,* but upon the amount *distributable.* The case does hold that, under the particular provisions of the very elaborate trust deed there involved, the trustee was not authorized to maintain a depreciation reserve. It does not deal with the general proposition in this connection on which the court asked for briefs; that is, whether, in the absence of specific directions, the duty to maintain a depreciation reserve will be implied where a trustee, under a residuary trust, makes a purchase of depreciable property. We submit that this case does not sustain petitioner's claim on either of the points to which these reply briefs are directed.

Codman v. Commissioner, 50 F. (2d) 763 (Pet. Br. pp. 20-21, note; Pet. Rep. pp. 11-12), arose out of the same transaction as *Codman v. Miles* (*supra,* p. 42). The same points there decided were reaffirmed. As we have seen, they have nothing to do with either of the points on which this court requested these briefs. This last decision did go further. In doing so, however, it discussed in no way the construction of Section 219 of the Revenue Act of 1921, for which petitioner cites it here. There is some discussion of the terms of the trust agreement and the court holds that under it no depreciation reserve was required. It has no bearing upon the question of testamentary construction involved in the case at bar (*supra,* pp. 2-18).

Roxburghe v. Burnet, 58 F. (2d) 693, and *Roxburghe v. The United States,* 64 Ct. Cls. 223, (*supra,* p. 37; Pet. Br. pp. 20-21, note; Pet Rep. p. 15), are also distinct. The cases arose under the Revenue Act of 1918 and could not assist in the construction of Section 219 of the Revenue Act of 1921, in connection with which it is cited here. The Court of Claims, however, construed the 1918 Act just as we now insist the corresponding provisions of the 1921 Act should be construed:

> "Subsection (b) of section 219 in providing for an additional deduction in computing the net income of the estate or trust refers to 'the will or deed creating the trust,' showing that reference must be had to the instrument creating the trust in ascertaining

> the distributive share thereunder. * * * The statute does not attempt to enlarge this interest or increase her distributive share. The amount of it is not in dispute'' (p. 228).

The decision of the Court of Appeals is quite similar. So far, therefore, as the construction of Section 219 is concerned, the case cannot sustain petitioner's claim; like the cases we have cited, it holds definitely that the test is the amount *distributable.* On the question as to whether the trustee was obliged to maintain a depreciation reserve, what the amount distributable was, the case can be no authority whatsoever because, as we have seen "the amount of it is not in dispute.'' The very issue which exists here (*supra,* pp. 2-18) as to the duty of the trustee was not raised at all in the *Roxburghe* case.

To the same effect petitioner cites

> *Crilly v. Commissioner,* 15 B. T. A. 642 (Pet. Rep. p. 12, note).

In that case the trustee distributed the depreciation reserve. The propriety of this distribution was not questioned or presented in any way. The Board neither passed upon the question of the construction of Section 219 of the Revenue Act of 1921, for which petitioner cites the case here, nor upon the question as to the duty of the trustee to maintain a depreciation reserve, the other point upon which this court requested briefs. The case has no bearing whatever on the case at bar, except for the fact that the opinion is by Mr. Marquette, who wrote the majority opinion below (R. 42-49) and evidently did not think there was any inconsistency in that opinion and what he said before in the *Crilly* case.

In the same note petitioner cites

Detroit Trust Co. v. Commissioner, 16 B. T. A. 207.

The case raises no question of depreciation or of the construction of Section 219 of the Revenue Act of 1921, in which connection petitioner cites it. The only question passed upon is that of the right of an equitable life tenant of a mining property to claim a deduction for depletion. The decision is based upon the *Fleming, Merle-Smith* and *Fowler* cases, 6 B. T. A. 900, 11 B. T. A. 254 and 11 B. T. A. 265. These cases have been reversed by the Circuit Courts of Appeal.

Merle-Smith v. Commissioner, 42 F. (2d) 837;

Fleming v. Commissioner, 50 F. (2d) 1075.

See also

Merle-Smith v. Commissioner, 22 B. T. A. 378.

The Detroit case is simply wrong.

Goff v. Commissioner, 18 B. T. A. 283 (Pet. Rep. p. 12, note), is another depletion case. It also is based upon the *Fleming, Merle-Smith* and *Fowler* cases, subsequently reversed (*supra*), and upon the *Detroit Trust* case (*supra*). It is also wrong. It does not deal in any way either with the question of depreciation or with the question of the construction of Section 219 of the Revenue Act of 1921, for which petitioner cites it here.

White v. Commissioner, 23 B. T. A. 391 (Pet. Rep. p. 12, note), is the same case as that in which we cited the subsequent opinion, *White v. Commissioner,* 25 B. T. A. 243 (Res. Br. p. 53). It sustains everything we have said on either of the two points on which the court has asked briefs. That case related to trusts under a residuary clause. Part of the trust assets were leaseholds. The trustees amortized the value of the leases over their remaining life, and submitted their accounts to the Surrogate's Court. The Surrogate's Court approved their accounts, including the provision for amortization. The Commissioner sought to increase the taxable income of the beneficiaries, by adding the amount of this amortization. Both in the earlier opinion, which petitioner now cites, and in the later opinion the Board cited Section 219 of the Revenue Act of 1921 and held that the controlling thing was the amount distributable, rather than the amount actually distributed (23 B. T. A. 397; 25 B. T. A. 249). In the earlier decision, which is the one petitioner now cites, the Board concluded that under the terms of the trusts and certain New York decisions, which it cited, the amortization deduction was improper. It refused to follow the order of the Surrogate's Court,

> "since it does not appear that an issue was raised as to the correctness of the trustees' action" (23 B. T. A. 400).

This result was directly contrary to the later decision of the Board, upon which we have relied. In the later decision the Board held the amortization deduction properly made and overruled the Commissioner's contentions. The Board seemed to regard the decision of the Surrogate's Court as binding on it (Res. Br. p. 53). At any rate, it held that the local law was applicable, and followed the local law regarding leaseholds, citing particularly *In re Golding,* 216 N. Y. S. 593, one of the cases upon which we relied in regard to leaseholds (Res. Br. p. 14).

At the argument petitioner apologized for having cited a decision of a Cicuit Court of Appeals which had since been reversed by the Supreme Court of the United States (Res. Br. p. 47). We are quite sure, therefore, that if he had an opportunity he would apologize for having thus cited an opinion of the Board, which the Board itself had repudiated in an opinion to which we had already called the court's attention (Res. Br. p. 53). There is nothing, of course, in either of the opinions in this case which sustains, in any way, the construction of Section 219 of the Revenue Act of 1921, suggested by petitioner in support of which petitioner cited it.

Falk, et al., Executors v. Commissioner, 24 B. T. A. 299 (Pet. Rep. p. 12, note), is another depletion case. It deals in no way either with the construction of Section 219 of the Revenue Act of 1921, for which petitioner cites it, or with the matter of depreciation, on which the court also asked for briefs. It relies upon the *Detroit Trust* case (*supra,* p. 47), the *Goff* case (*supra,* p. 47), and the first decision of the Board in the *White* case (*supra,* p. 47). It recognizes that the *Merle-Smith* and *Fowler* cases (*supra,* p. 47) had been overruled, but feels in some way that the decision overruling them is to be distinguished because of something said in the first *White* case (*supra,* p. 47). Petitioner advises that the case is pending in the Circuit Court of Appeals (Pet. Rep. p. 12, note). At any rate, it need not detain us as it is no authority for any point in which we are now interested.

We submit, therefore, that petitioner has produced no authority.

3. THERE IS NOTHING IN THE MISCELLANEOUS POINTS DISCUSSED BY PETITIONER.

Renewing his contention that the question is one for the application of federal law rather than state law (Pet. Rep. pp. 12, 13), the petitioner questions

> "just where respondent stands upon this proposition" (Pet. Rep. p. 13, note).

It can do no harm to repeat. The rights of the parties under the Whitcomb will are, of course, determined by the law of California (Res. Br. pp. 35, 36), by whose courts alone their rights are enforceable (Res. Br. pp. 38, 39). On the essential point, however, the duty of a trustee in cases of this kind to maintain a depreciation reserve, the federal law is the same as the California law (*supra,* p. 17; Res. Br. p. 27). Petitioner has never shown that the federal law was any different from the state law (Res. Br. p. 60; *supra,* p. 17). We have, therefore, said that for practical purposes petitioner's claim that the federal law governs "*may* well be granted." By this we mean just what we say; not that we do grant any such claim, because we know the contrary.

Petitioner characterizes as a suggestion, rather than a contention (Pet. Rep. p. 13) our position in this case as to the conclusiveness of the supposed federal law about this "*testamentary* trust of *real property*" (Res. Br. p. 35). That our position is fully supported, even by the authorities upon which petitioner relies, is made clear by the consideration that the passages which we have quoted from those authorities are taken from the quotations made from them in petitioner's own brief (Res. Br. p. 35). The administration of the federal income tax nearly always requires a consideration of the local laws. No one except a federal employee or contractor can earn any income without being dependent in some way upon local law. In applying the federal tax we must consider what substantive rights and obligations have arisen under the local law. Having ascertained those rights and obligations we must then consider the federal law in order to determine whether or not creation of these rights and obligations has resulted in that which the federal law regards as taxable income. The community property income tax cases were instanced, as example of the extent to which local laws must be examined in applying the federal income tax (Res. Br. p. 36). Another instance is the recent decision of this court in *Commissioner v. Caroline E. Burke, et al.*, decided November 28, 1932.

In this connection, petitioner refers to *Burnet v. Harmel,* decided by the Supreme Court of the United States November 7, 1932 (Pet. Rep. p. 14), as an authority against what we have said. The case illustrates very pointedly just what we have said. The necessity of looking to the state law in order to determine the nature of the rights and obligations of the parties to an oil lease, such as involved in that case, was the very thing determined by *Group No. 1 Oil Corporation v. Bass,* 283 U. S. 279 (Res. Br. p. 36). The *Harmel* case takes pains to recognize the correctness of the *Group No. 1* case. All the *Harmel* case does is, after having ascertained the parties' rights and obligations under the state law, to apply the conceptions of the federal income tax law to those rights and obligations in order to determine the amount and incidents of the tax.

> "The State law" says Mr. Justice Stone, "creates legal interests but the Federal statute determines when and how they shall be taxed."

We have already cited (*supra,* p. 16) an early ruling of the Commissioner which lays down just this distinction and correctly points out the necessity of considering the local law and the extent to which the local law shall be considered. The Commissioner pointed out that in trusts, gains from the sale of capital assets are considered income for income tax purposes, but frequently are not considered income by the state courts for the purpose of apportioning income and principal between life tenants and remaindermen. On the question of taxability he said:

> "As to this, however, the Federal statute and not the rule of probate law must govern. Decisions as to income and capital in other fields of law are not necessarily followed for income tax purposes. * * * The decisions of the local courts, however, as to the distribution of such items of income are important. They determine by whom the income should be accounted for. This makes it necessary that the distributable income be treated under class (4) and the capital gain or stock dividend under class (3) of section 219 (a)" (O. 1013, 2 C. B. 181, 183, 184).

Petitioner repeats (Pet. Rep. p. 14) his charge that the decree of the probate court was "a consent judgment." All we can do is to repeat what we have said (Res. Br. pp. 28-29, *supra,* p. 14) that there is nothing whatever in the record to support the statement that the order was obtained by consent.

In regard to the binding effect of the state court's decree petitioner attempts to distinguish *Uterhart v. United States,* 240 U. S. 598 (Res. Br. pp. 46, 55, 59; Pet. Rep. p. 14). As we understand this paragraph, the only distinction that we can see that petitioner suggests is that in the *Uterhart* case it was

> "very properly admitted by the Government that the New York decree is in this proceeding binding with respect to the meaning and effect of the will" (p. 603).

The court's emphatic statement as to the propriety of this admission was supported by its argument:

> "The right to succeed to the property of the decedent depends upon and is regulated by state law (*Knowlton v. Moore,* 178 U. S. 41, 57), and it is obvious that a judicial construction of the will by a state court of competent jurisdiction determines not only legally but practically the extent and character of the interests taken by the legatees" (p. 603).

The only distinction that can be suggested is that in the *Utterhart* case the government *very properly admitted* the binding effect of the state decision, while in this case the government quite *improperly seeks to reject* the state court decision.

Still attacking the decision of the probate court, petitioner repeats the citation of *Fidelity & Columbia Trust Co. v. Lucas,* 52 F. (2d) 298, and *Ford v. Commissioner,* 51 F. (2d) 206 (Pet. Br. pp. 32-37; Res. Br. pp. 41-46; Pet. Rep. pp. 14-15). As petitioner makes no further argument in support of the citation of these cases, and does not attempt to meet what we have said, there is no occasion for us to say more.

As a new authority on the same point, petitioner cites *Jackson v. Smietanka,* 272 Fed. 970 (Pet. Rep. p. 15). There is no doubt that the particular fee of $100,000 there in controversy was received by the taxpayer in 1918, and that when received it was received as compensation for personal services. There never was any claim by any party that the taxpayer was under obligations to refund the money. His only argument was that the money was income for years other than those in which it was received. The only support for this argument was an *ex parte nunc pro tunc* order. Contrast that case with the case at bar. In the *Jackson* case the order adjudicated no rights in controversy between any parties, since its only effect was to purport to allocate the compensation from one year to another. In the *Whitcomb* case the order adjudicated matters seriously in controversy between the parties and resulted in a judgment requiring the ultimate payment of over $600,000. In the *Jackson* case the petition was heard *ex parte.* In the *Whitcomb* case the question was submitted in the ordinary way after having been actively litigated between the parties at interest.

Petitioner attempts to distinguish *McCaughn v. Girard Trust Co.,* 19 F. (2d) 218 (Res. Br. pp. 47-50, 55; Pet. Rep. pp. 15-16). Apparently, petitioner concedes that the distinction is ''practical'' and not ''legal.'' The ground suggested is that ''obviously the distribution under an invalid will would pass no sort of title'' (Pet. Rep. p. 16). So also here the distribution of money, which distribution was not authorized in any way by the will, could pass no sort of title.

There is no attempt to distinguish any of the other cases cited by us on this question of the effect of the decree of the probate court (Res. Br. pp. 47-53, 54-56). The situation with regard to this order is very simple. As we have shown (*supra,* p. 52), federal income tax is based upon the application of federal laws to the rights and obligations conferred upon parties by state laws. While, so far as the federal government is concerned, proceedings between citizens in the state courts are *res inter alios acta* and not binding upon the federal government by any sort of doctrine of *res judicata,* nevertheless, those judgments do give rise to rights and obligations, upon the creation of which the federal income tax becomes due. The income tax cannot be computed without considering these extraneous facts. For example, a corporation operates a motor vehicle in the course of its business. The motor vehicle collides with a pedestrian. The pedestrian sues, alleging negligence, and gets a judgment. The corporation pays the judgment. The corporation deducts the payment as a business expense on its income tax return. Quite truly, the judgment is *res inter alios acta* so far as the United States is concerned; quite truly, it is not binding upon the United States in the sense of *res judicata;* nevertheless, the nature and character of the payment made by the corporation cannot be ascertained without looking at the judgment. The nature and character of the payment being ascertained, it remains a federal question whether such payment is a deductible expense. Before that federal question can arise, however, the judgment must be considered and must be given full credit.

Apparently the portion of the reply in which *Lewis v. Reynolds,* 284 U. S. 281 (Pet. Rep. p. 16) is cited is intended to pursue the same argument we have already discussed as to the possibility of some claim of the United States for additional taxes from the trustee having been barred by the statute of limitations (Pet. Rep. Br. p. 9; *supra,* pp. 35-36). Petitioner is mistaken in citing the case as authorizing the government to "set off taxes actually due against the amount of the refund claimed" (Pet. Rep. p. 16). The sense of the decision is that for each income tax year there is one tax for each taxpayer; that the taxpayer cannot assert a claim for refund without requiring an entire recomputation of the tax for that year; that if such recomputation shows that, owing to another error different from that upon which the refund claim is based, an error which had favored the taxpayer rather than the government, the tax originally paid had in fact been less than the correct tax due from the taxpayer, then no refund could be obtained. The principle is quite different from that of set-off. At any rate, it has no bearing on the case at bar. The only error in regard to the computation of any tax which is before the court in this case is that due to the insistence of the petitioner upon the addition to decedent's income of the amount of the depreciation reserve. At no time has it been alleged that there was any error in the computation of the trustee's tax. The record shows that everything which the trustee received was distributed to the beneficiaries (R. 121-122, *supra,* p. 30); that there could not have been a tax upon the trustee. The whole suggestion is foreign to the facts of this case and to the record before the court and to the two specific questions upon which the court asked briefs.

Finally, petitioner cites *Woolford Realty Co. v. Rose,* 286 U. S. 319, 330 (Pet. Rep. p. 16). That case has nothing to do with either of the two questions upon which the court asked briefs here. Petitioner cites it merely as authorizing the decision of tax cases upon some ground of expediency. What Cardozo, J. said there was that tax statutes are not to be construed in such a way as to give results obviously inexpedient. Petitioner has not shown any particular question of expediency involved in the instant case. It is, of course, expedient that the government derive revenue from taxes, but it is vastly more expedient that the courts and administrative officials administer tax laws justly and in accordance with their provisions and the rights of the parties. This, therefore, cannot be what petitioner means. The only matter of construction to which the remark of Cardozo, J. could be applicable is that regarding Section 219 of the Revenue Act of 1921, upon which this court asked briefs. We have shown that the construction for which petitioner contends would have one inexpedient result; it would permit taxpayers, who were parties to testamentary trusts, to make distributions of income in violation of the trust provisions and thereby reduce their income taxes (*supra,* p. 35). Any argument on the ground of expediency, therefore, must turn against petitioner.

Petitioner's last sentence imputes to respondent a desire "to escape taxation * * * by pursuing a particular course of conduct an indefinite number of years later'' (Pet. Rep. p. 16). This misconceives the entire case. Our argument is that, not because of any conduct on the part of ourselves or any other parties, the rights and obligations of the parties to the Whitcomb trust were fixed in the last century when that will was made and the estate distributed to the trustees. The fire of 1906, some fifteen years before the period here in controversy, necessitated certain changes in the administration of the trust which gave rise to investments in depreciable property and created the obligation on the part of the trustee to maintain a depreciation reserve. That obligation was recognized by the Board of Tax Appeals in fixing the amount of the tax here. Nothing done by any one at any subsequent time could, or did, affect in any way either the rights of the parties in regard to the income from 1921, or the amount of tax due from them on account of the receipt of that income.

III. SUMMARY.

In this case there are no questions of fact. It must turn on two propositions of law. The first proposition is that under Section 219 of the Revenue Act of 1921, respondent's decedent was taxable upon the amount of the trust income *distributable* to her during the fractional year involved (Res. Br. pp. 3-6; *supra*, pp. 18-49). The second proposition of law is that where, as here, a trustee under a residuary devise or bequest invests in wasting assets, the amount of income distributable to the beneficiaries is subject to a proper deduction for amortization (Res. Br. pp. 6-25; *supra*, pp. 2-18).

The first of these points was apparently conceded in petitioner's opening brief (*supra,* p. 29). It was only at the oral argument that, as an entirely new proposition, he suggested the construction for which he contends now.

The second of these propositions was entirely ignored in petitioner's opening brief (Res. Br. p. 25).

At the oral argument the court asked petitioner whether he knew of any authorities in support of the positions then and now taken by him on these two propositions. He was given leave to cover the two points in a reply brief. He certainly did not say then that the cases already cited in his opening brief were thought by him to sustain the positions he was taking on these two propositions. Pursuant to the leave of the court he has filed a reply brief. A quarter of it (Pet. Rep. pp. 12-16; *supra,* pp. 50-58) is frankly devoted to questions other than the two on which briefs were directed. While included under captions of the two questions upon which the court asked for briefs, more than half the rest (Pet. Rep. pp. 3-6; *supra,* pp. 9-17; Pet. Rep. pp. 8-12; *supra,* pp. 31-49), has manifestly no relation whatever to the captions under which it stands. Petitioner has not offered any single new authority tending to sustain his position on either of these two questions. On both of these two questions he relies upon a group of cases cited in his opening brief. In view of what he said at the oral argument, his present claim that these cases sustain his positions on these two points is clearly an afterthought (*supra,* pp. 18, 41). That the cases in question do not sustain his position on either of these two points is shown by the analysis we have made of them (*supra,* pp. 41-46).

On these two points, however, we respectfully submit that the demonstration made in our brief is sound (Pet. Br. pp. 3-25), that the authorities there cited support fully what we have said and that the discussion at the oral argument and in these reply briefs only confirms the soundness of the position originally taken.

Dated, San Francisco, California,
December 28, 1932.

Respectfully submitted,

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V. K. Butler, Jr.,
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Pillsbury, Madison & Sutro,
Of Counsel.

ASSESSMENT OF INCOME AND PROFITS TAX

December 29, 1932.

In pursuance of the provisions of existing Internal Revenue Laws James Otis, Trustee under the Will of A. C. Whitcomb, deceased, a taxpayer of 310 California Street, San Francisco, California, and the Commissioner of Internal Revenue hereby consent and agree as follows:

That the amount of any income, excess-profits, or war-profits taxes due under any return (or returns) made by or on behalf of the above-named taxpayer for the taxable year (or years) 1921, under existing acts, or under prior revenue acts, may be assessed at any time on or before June 30, 1934, except that, if a notice of a deficiency in tax is sent to said taxpayer by registered mail on or before said date, then the time for making any assessment as aforesaid shall be extended beyond the said date by the number of days during which the Commissioner is prohibited from making an assessment and for sixty days thereafter.

James Otis,
Trustee under the Will of
A. C. Whitcomb, deceased,
Taxpayer.

[SEAL*]

By

Commissioner.

By ______ ______
(Date)

*If this consent is executed on behalf of a corporation, it shall be signed with the corporate name, followed by the signature and title of such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition to which the seal, if any, of the corporation must be affixed. Where the corporation has no seal, the consent must be accompanied by a certified copy of the resolution passed by the board of directors, giving the officer authority to sign the consent.

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